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# THE FALLACIES OF PROTECTION

BY HENRY HERZBERG

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AT last the long-suffering "ultimate consumer" is in rebellion. The mounting cost of living has at least one virtue in concentrating public attention upon the workings of our tariff laws. Though the causes which contribute to the inordinate high prices of commodities are not understood thoroughly even by economists, yet there is a popular belief that our indefensible tariff is responsible for the progressive increase of living expenses by stifling foreign competition and enabling our producers to advance prices artificially without regard to the demands of the market.

At any rate, the masses are seeking light upon this absorbing question and are inclined to inquire as to the policies for which the political parties of to-day stand. In one case a tariff is urged which is to be levied for purposes of revenue only—a tariff which shall furnish ample revenue for all the needs of the Government, but shall provide no incidental "protection" to the producer or distributor.

In the other instance taxes are imposed so high as to prohibit importations regardless of whether such prohibitions actually check the flow of revenue or whether our industries are controlled by oppressive combinations. The domestic manufacturer and distributor, whether efficient or inefficient, whether or not he is conducting business antagonistic to sound public policy, must be protected from foreign competition. Let us inquire briefly as to the practical effects of these two opposing policies.

A tariff for revenue only tends toward an economically administered Government because it approaches equality of treatment respecting classes and trade and hence discriminates neither for nor against any section or class. It is a foe to favoritism and special privilege, and therefore does

not open the door for political bargaining. On the other hand, protective duties ultimately produce a riot in governmental extravagance by reason of the power to "protect" industrial interests which leaves room for political debauchery. It is this character of tariff legislation which has degraded the law-making function of the Government. Instead of using the arm of the Government to protect the commonwealths against adverse legislation, Senators and Representatives urge discriminating laws in favor of particular industrial interests. The imposition of tariff charges, which should be designed solely to produce revenue for the necessary expenditures of the Government, has set into motion almost countless demands for the granting of bounties to special groups and the enactment of discriminating laws for certain classes. Thus by a system of favors and privileges the Government in effect guarantees profits to private interests and may be said to be in partnership with the same without, however, the power of regulation or control.

A tariff for revenue is inclined to impose no duty on any article above the lowest rate which will yield the largest amount of revenue and would subject luxuries to the maximum revenue duty. Protective duties subordinate the question of revenue to the matter of safeguarding the gains of producers; and hold common every-day necessities to be no more exempt from the blight of high taxation than luxuries in which only the privileged few can indulge. A tariff for revenue would reduce the tariff to a basis where the domestic manufacturer must meet competition. Protective duties guard the home producer from foreign competition and of necessity are committed to the guarantee of profits. The one upholds the American doctrine of self-help, encourages individual initiative, and entices enterprise to engage in healthy competition for the rewards of domestic and foreign commerce. The other supports the principle of paternalism which extends Government aid for private purposes—a policy which, as will be seen presently, suppresses competition and leads either to industrial inefficiency or to the crushing of the small producer.

From whatever angle that we view the question of taxation there can be but one conclusion: that a high tariff levied for purposes over and beyond the needs of an economically administered public service is unmoral. It is, in

fact, nothing other than a tribute or a gratuity in which inheres oceans of possibilities for extortion, monopoly, industrial persecution, and abridgment of individual liberty.

Through this Government bounty the consumers are forced to pay a tribute to a legally protected class. In other words, the holy arm of the law is invoked to suspend, or at least arrest, the operation of competition among domestic producers and through this statutory interruption, so to say, of competition the consumers of the land are compelled to pay taxes which are levied purely for private purposes.

Legislation which discriminates against or in favor of any economic or social group is vicious, not only because it clothes those of one station with a sort of quasi-legal power to tyrannize over those of other ranks, but also because taxes laid for private purposes are clearly a prostitution of governmental functions.

A republican form of Government is designed, as Madison expressed it, to dispense "equal and exact justice." A "protective" tariff, so called, is simply a fiscal tribute exacted by special interests and is a signal instance of perverted governmental authority. It needs no argument to show that there is no warrant in the taxing clauses of the Constitution of the United States to aid private enterprise at the expense of the whole people. When a statute has the effect of prohibiting imports such a law protects private industries by indirection and is in contravention of the Constitution. The legal principle is unassailable that a tax which is laid for a private purpose is null and void.

But, lamentably, the court would not be warranted in construing a law as intending to effect the prohibition of imports when an act upon its face purports to raise revenue.

But even if protective duties be technically within the bounds of constitutional law, yet the taxing power is defiled when the Government by "a decree under legislative forms" (an expression used by the Supreme Court in a noted decision) protects individual or corporate producers in despoiling the common people or the whole body of consumers of the land of their private property. By whatever devices the tariff be disguised, whether by minimum or maximum provisions, "compensatory" features or other schemes, it still remains a fact that in the end it is a tax upon consumption which cannot be shifted by the consumer. No amount of sophistry can distort the fundamental truth

that a people cannot be taxed into prosperity. The higher the tariff, the greater necessarily is the burden sustained by the masses, and it follows that the general well-being perforce is influenced adversely by the imposition of high taxation because a lessened purchasing power must needs lower the standard of living.

That a high tariff is a privilege granted by law to special interests and that the practical result of this law-created privilege is to raise the price of the daily necessities of life can be shown clearly enough.

Limited space will permit only a few illustrations to prove that protective duties are plainly a tax on living. Follow the course of the tax on foreign wool from the importer to the retail buyer of clothing. In this case each successive process of manufacture demands a profit by reason of this tax privilege. The importer claims 10 per cent., the spinner 15 per cent., the weaver 25 per cent., the retail clothier 50 per cent., and in the end the increase in the cost of the suit, starting with the tariff tax of \$1.93, reaches the total of \$5.66. Not only are tariff taxes laid on the raw materials, but corresponding "compensatory" taxes are placed on the finished products of manufacture. The result is that the class which can only pay a low price for clothes do not get wool; they get shoddy and cotton, which do not yield nearly the same warmth nor do they last one-fifth as long.\* Wearers of wool and wearers of cotton with every purchase make a gift to a consolidated industry or, in other words, are taxed for an inferior article in order to protect these combinations from competition.

The Tariff Board in its official report stated that on samples of sixteen pieces of cloth, taxed 184 per cent. in the tariff, the prices in the markets of the United States were 67 per cent. higher than the prices for the same articles in Europe.†

Despite the tribute which the consumers must pay to the mill-owners and distributors of wool and woollen fabrics, the salaries paid the workers are extremely meager.‡ More-

\* This estimate is based on a contribution by Hon. William C. Redfield, *New York Times*, October 11, 1910.

† See Synopsis of Report of Tariff Board on Schedule K on Wool and Woolens, page 9.

‡ See Report of United States Commissioner of Labor, Charles P. Neill, Senate Document No. 870, Sixty-second Congress, Second Session.

over, the industry has made little progress and, in fact, to-day is languishing though the duties have remained practically unchanged for forty years.

A review of the cotton industry\* would disclose like enormities which are fostered by our prohibitive tariff. Unquestionably the total labor cost in cotton fabrics is only a fraction of the excessive tariff. In a number of cases the duties levied are three times the total labor cost.

In like manner scarcely a household article escapes the grasping touch of the Protectionist. Chinaware, earthenware, glassware, mattings, as well as carpets, cutlery, chairs, tables, desks, ornaments, wall-paper, sewing-machines, medicine, and what not, all are subject to the steep rates of custom duties. Take the case of sugar. The United States Treasury derives about \$50,000,000 out of the tax on sugar, but on the sugar produced in the United States the Government does not obtain a single cent, while at the same time about \$60,000,000 is bestowed upon producers as a gratuity. By virtue of the tariff on sugar, the American people are forced to pay \$110,000,000 annually upon this table necessity, or at the rate of \$7.25 for each family.

Again, let us consider the relation of the farmer as a producer to the high cost of living and also note his own economic status by reason of protective duties.

We may allow safely that some of the factors which contribute to the rise of commodities' prices are an augmented gold supply, excessive governmental expenditures which dissipate vast capital and lessen the nation's productive power, the wasting of natural resources which may have lowered the prices of living necessities of a previous generation at the expense of this generation, the lack of intensive farming, and the shortage of domestic farm produce and live-stock.

It would be unfair, then, to attribute the rise in the prices of food products wholly to our high tariff. We should hold the farmer largely responsible because of his inefficient and antiquated agricultural methods and also should adjudge our merchants blameworthy for the wastefulness of our distributive processes. Likewise, the phenomenal growth of cities and the consequent demand for urban labor is accountable, in part, for the increase in prices of farm products.

\* See articles in *New York World*, by Robert Kenneth MacLea, September 5, 1912, and August 12, 1912. Mr. MacLea was the former expert of the Tariff Board.

But aside from these forceful influences, we must look to our tariff laws to furnish a key which will unlock some of the secrets of the high cost of living.

Protective duties penalize both the farmer and the consumer for the use of daily commodities. There is this difference, however, as we shall see, in that the farmer can recover part of the fines, at least, while the consumer is helpless. For example, the agriculturist is dependent largely upon manufactured iron and steel products and lumber for his working utensils and tools. The importer advances, say, twenty per cent. in the increased price due to the tariff, the jobber adds an increase of twenty-five per cent. on the importer's price, and the retailer advances his figures thirty-three and one-half per cent. over those of the jobber. These prices would have to be paid by the consumer if he used imported goods. As it is, foreign competition is legally stifled by the medium of the tariff, while domestic competition is illegally throttled by the means of combinations. So it happens that when the farmer buys domestic iron and steel products he is forced to pay an artificially increased price at retail about equal to twice the amount of the tariff tax.

But there is compensation for the farmer, as he receives large returns for his limited crop yields. In measure, at least, he can transfer the tariff tax to the purchaser of his grains, and the distributor in turn unloads it upon the consumer. Alas, the ultimate consumer must sustain the tax which is originally borne by the producer, as well as the tax on all competition in so far as all classes are able to shift taxes to the final users of commodities.

This being the case, is not the taxation of imported food products the quintessence of folly?

With our tremendous increase of population, our lack of intensive agricultural methods, and the tendency to urban concentration with the large mass of the people employed as distributors rather than producers, and when our food consumption threatens actual production, is it not stark madness to increase the cost of daily food by maintaining artificial barriers against imported supplies?

We must recognize the fact that high tariff arbitrarily retards the free operation of enterprise if it does not directly throttle competition and dislocate the world's supply and demand, and prevents the interaction of international eco-

conomic forces. If this were not true the price level of commodities as indicated by the scientific index price of authorities\* would not be decidedly higher in the United States than in European countries. The scarcity of American food products, however real, is an artificial shortage because protective duties debar us from enlarging our market by shutting out wholly or in part the world's supplies. The diminution of the supply not only raises the price of the foreign commodity to the extent of the tariff tax of duty, but advances the price of the American products to the same price level and permits combinations to control the market by an artificial scarcity.

But even in the case of manufactured goods where there is not a shortage, but an actual surplus due to greater productiveness and abundance, the tariff aids corporate enterprise to manipulate the output in the same manner as if there were a real deficit in production.

Of the \$15,000,000,000 worth of domestic manufactured products consumed in the United States the Government annually receives revenues amounting to about \$3,000,000, while it is estimated that the producers receive a bounty of millions or even billions of dollars in the form of a margin of protection. Whether this sum is actually so vast only an expert can determine, but that it is prodigious there can be no question. Suffice it to say that by the most liberal computation the consumers virtually are dispossessed of vast treasure through legislative decrees. The tariff then invalidates such factors as improved transportation facilities, heightened processes of production and distribution and inventions which, under the play of competition and without Government interference, would tend toward abundance and falling prices. Instead of our industries affording large profits and wages through an enlarged productive power, our producers and distributors through the medium of protective duties exact "unreasonable" profits by curtailing production and maintaining scarcity of products at a high price.

"Protection" is, in fact, what the great Cavour denomi-

\* See the Lodge Senate Majority Report No. 912 on "Wages and Prices of Commodities," page 23, Part I., Sixty-first Congress, Second Session. Reports of Consuls Griffiths and Ingram, Senate Document No. 477, pp. 15, 16, 19, Part I., and pp. 63-67, Part III., Sixty-first Congress, Second Session.



nated it: "the most insidious form of privilege," and in the most practical way it is the friend and champion of special privilege by constricting the markets from which the masses must buy their daily necessities for household and personal uses and levying a tribute upon every man, woman, and child in the land.

For decades the cry went forth that labor must be protected from foreign competition and that a high tariff is essential to equalize the difference between the cost of domestic and foreign productions.

Though it is common knowledge that the rates are greatly in excess of this difference and that in many cases the duties are prohibitive, nevertheless the theory is advanced that a tariff rule must be based upon the disparity in the cost of foreign and domestic manufactures so that "reasonable profits" may accrue to "American industries." We have shown previously that this cannot be claimed to be a constitutional rule for raising revenue. On the contrary, it is merely "protection" in a new garb or paternalism in an old form. It is levying taxes so as to stimulate profits to certain producing classes at the expense of the consuming public.

We should understand that a tariff board created to ascertain the difference between the cost of production at home and abroad and to condition the degree of gain which the Government could guarantee to the producer would be a snareful delusion for the persuasive reason that accurate cost prices, according to the opinion of experts, are not obtainable by the most painstaking investigation. The fallacy of conditioning a tariff upon the rule to which we have referred has been exposed by Professor Taussig. In a well-knit argument he holds that "if carried out to the full" this principle "would lead to the utmost extreme of protection" and if "applied with consistency it would lead to a complete annihilation of foreign trade." He indisputably says that the equalization of cost of production means that the production of everything is to be encouraged, and where the difference in cost is great the duty is to be high, and if the disparity is small the duty is to be low, so that automatically the duty advances in proportion as the American cost price is large. The consequence is that the more unsuited the conditions are for economical and efficient production the more pronounced will be the tendency

toward protection. "Under this equalizing principle, the worse the natural conditions the more extreme will be the height of protection. . . . It is for this simple and obvious reason that the principle seems to me to be worthless for settling the tariff problem."

With penetrating touch Professor Taussig exposes the lack of foundation for the two prejudices that the domestic production of a given article is *per se* good and that high wages are the result of the tariff and cannot be maintained without the tariff. While admitting that economists are not "unanimous on the controversy between protection and free trade," yet he considers it a commonplace that "to make a thing at home is not to our advantage if we make it at high cost. To import it is not a source of loss when we import the thing more cheaply than we can make it at home." He says the economist holds that "when you try to equalize costs of production everywhere you induce the employer to turn to industries where labor is not efficient. The very fact that costs are high indicates that there is some cause of inefficiency. You divert labor and capital from the industries that are best worth while, diminish the general product, and so diminish the source from which all wages eventually come."\* In the main, the question of liberal wages depends upon the productiveness of industry, and therefore it is true that the efficient man is in reality cheap though he commands high wages.

Governor Wilson has pithily described the true source of wages, and his definition may also be applied aptly to the cost of production. He says: "Wages come from the intelligence and energy of the working-men, made effective by the presence of natural resources and their management by efficient managers."†

When conditions are unfavorable for economic and efficient production, no amount of protective duties will make such production efficient. In such cases the only effect of a high tariff is to raise prices artificially and to maintain the inferiority of antiquated plants.

To ascertain the difference in cost of production between foreign and domestic commerce no standard can be created

\*"The Tariff and the Tariff Commission," by Professor F. W. Taussig, *Atlantic Monthly*, December, 1910.

† Address by Governor Woodrow Wilson at the National Democratic Club, New York, January 3, 1912.

other than an arbitrary standard which is of no value. Shall we ascertain the cost of the most efficient or the least efficient mill?

The most efficient plant naturally can produce the best wares at the lowest cost, while the least efficient will produce the poorest goods at the highest cost. Surely the mill or factory which is best equipped and most ably managed requires no protection whatsoever. If, then, we reckon the cost of production according to the cost figures of the inferior plant, we add so much unnecessary profit to the superior producer, prolong the existence of the unfit, and artificially stimulate commodity prices to the consuming public.

As a matter of fact, not only are there differences in the cost of production between foreign and domestic manufactures, but perhaps no two American producers have cost sheets in which the figures are identical. The cost price of any given article depends upon varying factors, such as proximity of raw material and transit facilities to the factory, efficiency of labor, and managerial ability. Hence to afford protection to the efficient producer who requires no protection or to grant "reasonable profits" to the inefficient producer who is deserving of no paternal care will benefit neither capital nor labor. In summing up the argument against the imposition of a high tariff the following facts are dominant: There is no constitutional warrant for the Congress to guarantee profits on private industrial enterprises in exercising its lawful authority to raise adequate revenue for governmental needs; it is the function of governments to equalize opportunities, but not to promote inequalities.

To extend paternal aid to efficient producers who require no protection, or, on the other hand, to grant "reasonable profits" to inefficient producers, serves to increase the margin of profits for the superior manufacturer, prolongs the existence of the unfit producer, and artificially stimulates commodity prices which the consuming public must pay. In truth, the more unsuited conditions are for economical and efficient production the more pronounced is the tendency toward the policy of protection.

If industries be highly organized production will be efficient and wages will be high without protective duties, but if inferior technical equipment prevail and inferior labor

be employed high protective duties will not save an industry from deterioration. High wages are dependent upon productive efficiency, while low relative wages go hand in hand with poor equipment and a low standard of production.

Prosperity cannot be purchased by a governmental bounty; the well-being and substance of the individual can be created only by an enlarged productive power and a consequent improving wage scale.

To predicate a tariff upon differences in cost between foreign and domestic productions is as disingenuous as it is impossible of accomplishment. Absolute cost prices are not obtainable. Moreover, in the field of manufacture the selling price is not governed exclusively by the cost of an article. Under normal circumstances the selling price is controlled legitimately by competitive factors and supply and demand; but when normal economic conditions are interfered with by legislation which chokes foreign competition, then the forces of monopoly hold sway. In other words, protective duties artificially raise the selling price by arresting foreign competition and shutting out the world's supplies from American markets.

It is neither consistent nor just for the Government to regulate transportation companies and attempt to control the monopolistic tendencies of industrial combinations, while, at the same time, it is partial to concentrated capital by enacting tariff laws which permit producers to bar out effective foreign competition and raise the price level of commodities artificially.

It might be added that it is even more unjust for the Government to harbor artificial stimulation of prices by inequitable tariff laws than for monopolies in trade to crush their rivals and advance the cost of commodities, cruel as is this practice, since it is primarily the function of governments to equalize opportunities and not to promote inequalities.

HENRY HERZBERG.